REPORT OF EXAMINATION
OF THE

CARE WEST INSURANCE COMPANY

AS OF
DECEMBER 31, 2004

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San Francisco, California
April 6, 2006

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

CARE WEST INSURANCE COMPANY

(hereinafter also referred to as the Company) at its statutory home office located at 4020 Sierra College Boulevard, Suite 200, Rocklin, California 95677.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2001. This examination covers the period from January 1, 2002 through December 31, 2004. This examination included a review of the Company's practices and procedures, an examination of the management records, tests and analyses of detailed transactions within the examination period, and an evaluation of assets and a determination of liabilities as of December 31, 2004, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; and sales and advertising.

SUBSEQUENT EVENTS

Effective January 1, 2006, the Company switched to a new policy and claims system that is housed and operated at the Company's home office. The new system is developed by Fiserv and will be replacing the Remote Data Solutions (RDS) system. The conversion of the RDS data to the Fiserv system began on December 29, 2005. The Company stated that it had entered into two new agreements with RDS to help facilitate the transition to the new system. The first agreement will allow the Company and Pegasus to have inquiry-only access to the RDS data until such time as the Company elects to terminate access. The second agreement would have allowed the Company and Pegasus to return to the RDS system and process claims and policies the same way as under the original contract in the event that the Fiserv system is not fully functional by January 13, 2006. The Company has stated that the Fiserv system went live on January 3, 2006.

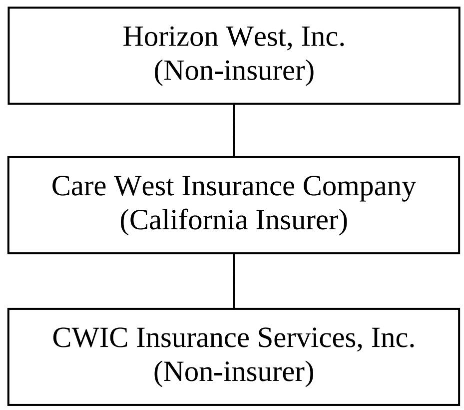
A review was made of the Company's general controls over its information systems, during the migration to Fiserv. Weaknesses were noted in the areas of disaster recovery/business continuity planning, data backup procedures, physical security, and management oversight of the information systems functions. The weaknesses noted were presented to the Company and it was recommended that the Company take measures to strengthen its information system controls. The Company stated that it has taken measures to address the concerns noted above.

COMPANY HISTORY

The Company was formerly a captive insurer domiciled in the State of Vermont. It reinsured risks related to workers' compensation policies issued by ceding carriers to skilled nursing homes and convalescent hospitals which were owned or operated by its parent, Horizon West, Inc. On December 5, 1996, the Company received its Certificate of Authority from the California Department of Insurance authorizing it to transact the workers' compensation class of insurance. On December 17, 1996, the Company redomesticated from Vermont to California. On December 31, 1996, the Company began writing the same workers' compensation policies on a direct basis.

MANAGEMENT AND CONTROL

The Company is a wholly-owned subsidiary of Horizon West, Inc., and a member of an insurance holding company system. The following organizational chart depicts the interrelationships of the companies within this holding company system as of December 31, 2004 (all ownership is 100%):



Management of the Company is vested in a six-member board of directors. The directors and the principal officers of the Company as of December 31, 2004 are as follows:

Directors

Name and Residence	Principal Business Affiliations
Larry W. Barefield Jr.* Bruce, Mississippi	President Western Care Construction Company
Martin A. Harmon Loomis, California	President and Chairman of the Board Care West Insurance Company
Martine D. Harmon Grass Valley, California	Property Manager Western Care Construction Company and Auburn Manor Holding Company
Mathew E. Harmon Roseville, California	Director of Land Development Western Care Construction Company and Auburn Manor Holding Company

Name and Residence	Principal Business Affiliations
James F. Schweder Carmichael, California	President and Chairman of the Board CWIC Insurance Services, Inc.
Donald T. Trowbridge Loomis, California	Chief Financial Officer, Secretary and Treasurer Care West Insurance Company and Western Care Construction Company

* Mr. Barefield was appointed to the board of directors in 2005 to fill a vacant position.

Officers

Name	Position
Martin A. Harmon**	President
Donald T. Trowbridge	Chief Financial Officer, Secretary and Treasurer

**Resigned as President in June 2005 and was replaced by James F. Schweder.

Management Agreements

Claims Management Services Agreement: Effective January 1, 2000, the Company entered into a second claims management services agreement for claims incurred on or after January 1, 2000 with Pegasus Risk Management, Inc. (Pegasus). Under the terms of the agreement, Pegasus administers the Company's claims operations, which include the adjusting and settlement of claims, investigative services, medical management services, and loss and statistical information services. Compensation is based on a fixed fee per claim.

As of November 30, 2004, Pegasus agreed to assume the handling of all open insurance claim files previously handled by the Company’s former claims administrator, Crawford & Company (Crawford). Pegasus was paid $1,000 per claim for the 35 remaining open claims that were transferred from Crawford. The Company paid fees of $97,350 to Pegasus for its claims management services in 2004.

Data Processing Services Agreement: On August 1, 1997, the Company entered into a data processing service agreement with Remote Data Solutions, Inc. (RDS). Under the terms of the agreement, RDS furnishes the Company with data processing services that include the use of computer equipment, computer programs, and other general support services. Compensation is based on a fee schedule included in the agreement. The Company paid fees of $109,071 to RDS for its data processing services in 2004.

Administrative Services and Other Benefits Contract: On January 1, 1997, the Company entered into a service contract with Western Care Construction Company, Inc. (WCCCI). Under the terms of this contract, WCCCI provides the Company with administrative, clerical, computer and accounting support services. The Company paid fees of $5,409 to WCCCI for administrative services in 2004.

Office Rental Agreement: On January 1, 2002, the Company entered into an office rental agreement with Auburn Manor Holding Corporation (AMHC). Under the terms of the rent agreement, the Company pays AMHC rent of $2,126 per month for its home office space. The Company paid rent of $25,522 to AMHC for 2004.

Client, Underwriting and Policy Service Agreement: On July 1, 1999, the Company entered into a client, underwriting and policy service agreement with CWIC Insurance Services, Inc. (CWIC). Under the terms of the agreement CWIC provides the Company with client, underwriting and policy services, which include: communicating and delivering policies and invoices to insureds; marketing the Company's products; underwriting policies; representing the Company in communications and obligations to the WCIRB; filing rate changes or premium modifications; developing policy forms and endorsements and submitting them to the proper regulatory agencies; and maintaining client files for the benefit of the Company. The Company paid fees of $72,000 to CWIC for its client, underwriting and policy services in 2004.

The Company is not in compliance with the California Insurance Code (CIC) Section 1215.5(b)(4) because it did not obtain prior approval from the Commissioner for its Client, Underwriting and

Policy Service agreement. It is recommended that the Company comply with CIC Section 1215.5(b)(4). This matter has been referred to Legal Compliance for follow up.

Safety and Loss Control Service Agreement: On August 1, 2003, the Company entered into a safety and loss control service agreement with CWIC Insurance Services, Inc. (CWIC). Under the terms of the agreement, CWIC provides safety and loss control services on behalf of the Company to its policyholders. These services include: developing a Safety & Loss Control Manual outlining systems and procedures for improving safety and loss control at the policyholder's location; performing on-site loss control surveys, record analysis and in-service training; and evaluating prospective policyholder's current safety and loss control systems to determine if they are an acceptable risk for the Company. The Company paid fees of $296,500 to CWIC for its safety and loss control services for 2004.

The Company is not in compliance with the CIC Section 1215.5(b)(4) because it did not obtain prior approval from the Commissioner for its Safety and Loss Control Service agreement. It is recommended that the Company comply with CIC Section 1215.5(b)(4). This matter has been referred to the California Department of Insurance (CDI) Legal Division for follow up.

Consolidated Federal Income Tax Allocation Agreement: Effective January 1, 1999, the Company entered into a tax sharing agreement with its parent company, Horizon West, Inc., in which the Company files a consolidated federal income tax return with its parent. Under the terms of the agreement, the Company is liable to the parent for the Company's allocated share of the parent's consolidated federal income tax obligation, and the parent is obligated to pay to the Company (or offset against future tax liabilities of the Company) any tax benefit that the parent has realized on its consolidated tax return as a result of losses the Company has experienced. This agreement was approved by the CDI on April 21, 1999.

TERRITORY AND PLAN OF OPERATION

The Company is licensed to transact workers' compensation insurance business only in the State of California. The Company's primary emphasis is on nursing homes. Direct premiums written were $15.1 million in 2004.

Since its inception in 1996, the Company has focused its writings primarily on policies for companies affiliated with its parent, Horizon West, Inc., a senior healthcare management organization. In 2004, the Company decided to expand its writings beyond its previous book of business by becoming a specialty writer of healthcare facilities. In March 2004, the Company contracted with an independent broker to produce non-affiliated business in this segment of the market for the Company. The Company contracted with an additional broker in June 2005.

LOSS EXPERIENCE

The Company reported operating results as follows during the examination period:

Year	Net Underwriting Gain of (Loss)	Net Income or (Loss)
2004	$1,918,138	$1,555,708
2003	3,988,229	3,176,529
2002	(4,530,037)	(3,573,505)

In 2002, the Company experienced a significant net underwriting loss and overall net loss. The Company adjusted its risk profile in 2002 by diversifying its business outside of California through a quota share reinsurance agreement covering targeted workers' compensation business in South Dakota and Minnesota. This business was written by First Dakota Indemnity Company and reinsured by the Company. The Company stated that it worked with its parent to institute a comprehensive internal risk management program in 2003 which helped reduced the number of indemnity claims in the subsequent years.

REINSURANCE

Assumed

Effective January 1, 2002, the Company entered into a quota share reinsurance agreement with First Dakota Indemnity Company whereby the Company assumed 50% of the gross retained liability and direct retained premium on workers' compensation and employers liability business written in Minnesota and South Dakota. Effective June 30, 2003, this agreement was terminated on a run-off basis.

As a captive insurance company in the State of Vermont, the Company reinsured risks related to workers' compensation policies issued to convalescent hospitals and retirement facilities related to its parent. Under the terms of the agreements, the Company reinsured all losses to a limit of $350,000 per occurrence for policy years 1990-1991 and 1993-1995, $250,000 for 1992, and $500,000 for 1996. The ceding carriers were National Union Fire Insurance Company (1989 – 1991), Transamerica Insurance Company (1991 – 1994), Firemen's Fund Insurance Company (1994 – 1995), and TIG Insurance Company (1995 – 1996). These agreements have been in run-off since 1996.

Ceded

Following is an outline of the Company's ceded reinsurance program as of December 31, 2004:

Type of Contract	Reinsurer	Company's Retention	Reinsurer's Maximum Limit
Excess of Loss			
First Layer	Aspen UK Limited – 20% Underwriters at Lloyd's of London – 80%	$1 million ultimate net loss each occurrence	$1 million excess of $1 million ultimate net loss each occurrence
Second Layer	Aspen UK Limited – 20% Underwriters at Lloyd's of London – 80%	$2 million ultimate net loss each occurrence	$3 million excess of $2 million ultimate net loss each occurrence
Third Layer	Aspen UK Limited – 20% Underwriters at Lloyd's of London – 80%	$5 million ultimate net loss each occurrence	$5 million excess of $5 million ultimate net loss each occurrence

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2004

Underwriting and Investment Exhibit for the Year Ended December 31, 2004

Reconciliation of Surplus as Regards Policyholders from December 31, 2001 through December 31, 2004

Reconciliation of Examination Changes as of December 31. 2004

Statement of Financial Condition
as of December 31, 2004

	Ledger and Non-ledger Assets	Non-Admitted Assets	Net Admitted Assets	Notes
Assets				
Bonds	$ 19,436,888	$	$ 19,436,888	
Common stocks	182,276	8,661	173,615	
Cash and short-term investments	14,972,489		14,972,489	(1)
Investment income due and accrued	416,591		416,591	
Agents' balances or uncollected premiums:				
Premiums and agents' balances in course of collection	813,370		813,370	
Deferred premiums, agent's balances and installments booked but deferred and not yet due	7,690,096		7,690,096	
Reinsurance:				
Funds held by or deposited with reinsured companies	354,750		354,750	
Net deferred tax asset	2,088,781	1,418,265	670,516	
Guaranty funds receivable or on deposit	144,298		144,298	
Electronic data processing equipment	12,718	12,718		
Furniture and equipment	316,994	316,994		
Equities in deposits in pools and associations	2,758		2,758	
Total assets	$ 46,432,009	$ 1,756,638	$ 44,675,371	
Liabilities, Surplus and Other Funds				
Losses			$ 21,927,701	(2)
Reinsurance payable on paid loss and loss adjustment expenses			142,642	
Loss adjustment expenses			2,638,675	(2)
Commissions payable			343,113	
Other expenses			374,119	
Taxes, licenses, and fees			249,885	
Federal and foreign income taxes			801,469	
Unearned premiums			7,998,564	
Ceded reinsurance premiums payable			176,314	
Excess of statutory reserves over statement reserves			2,145,000	(3)
Total liabilities			36,797,482	
Common capital stock		$ 1,000,000		
Unassigned funds		6,877,889		
Surplus as regards policyholders			7,877,889	
Total liabilities, surplus and other funds			$ 44,675,371	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2004

Statement of Income

Underwriting Income		
Premiums earned		$ 12,017,398
Deductions:		
Losses incurred	$ 7,198,500	
Loss expenses incurred	1,045,871	
Other underwriting expenses incurred	1,854,889	
Total underwriting deductions		10,099,260
Net underwriting gain		1,918,138
Investment Income		
Net investment income earned	$ 847,063	
Net investment gain		847,063
Other Income		
Miscellaneous income	$ 10,215	
Total other income		10,215
Net income before federal income taxes		2,775,416
Federal income taxes incurred		1,219,707
Net income		$ 1,555,709

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2003		$ 8,129,236
Net income	$ 1,555,709	
Change in net unrealized capital gains or (losses)	(7,849)	
Change in net deferred income tax	591,595	
Change in nonadmitted assets	(245,802)	
Excess of statutory reserve over statement reserves	(2,145,000)	
Change in surplus as regards policyholders for the year		(251,347)
Surplus as regards policyholders, December 31, 2004		$ 7,877,889

Reconciliation of Surplus as Regards Policyholders
from December 31, 2001 to December 31, 2004

Surplus as regards policyholders, December 31, 2001, per Examination			$ 4,738,372
	Gain in Surplus	Loss in Surplus	
Net income	$ 4,750,142	$	
Change in net unrealized capital gains	19,196		
Change in net deferred income tax	934,314		
Change in nonadmitted assets		655,177	
Change in provision for reinsurance	7,684		
Excess of statutory reserves over statement reserves		2,145,000	
Write-ins for gains in surplus	228,358		
Totals	$ 5,939,694	$ 2,800,177	
Net increase in surplus as regards policyholders			3,139,517
Surplus as regards policyholders, December 31, 2004, per Examination			$ 7,877,889

Reconciliation of Examination Changes
as of December 31, 2004

Account	Per Company	Per Examination	Surplus Increase (Decrease)	Notes
Excess of statutory reserves over statement reserves	$0	$2,145,000	$(2,145,000)	(3)
Net decrease to surplus, per examination			(2,145,000)	
Surplus as regards policyholders, December 31, 2004, per Company			10,022,889	
Surplus as regards policyholders, December 31, 2004, per Examination			$ 7,877,889	

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Cash and Short-term Investments

Certain cash and short-term investments are held in accordance with assumed reinsurance agreements for future payment of losses and loss adjustment expenses. Trust accounts were set up for each ceding carrier that the Company assumed business from during the periods of 1989 to 1996 and 2002 to 2003. All of these agreements are currently in run-off. Total invested assets that were held in these reinsurance trust accounts were $3.4 million as December 31, 2004.

(2) Losses and Loss Adjustment Expenses

A Casualty Actuary from the California Department of Insurance (CDI) reviewed the Statement of Actuarial Opinion and actuarial report prepared by the Company's independent actuary and concurred with the conclusion that the loss and loss adjustment expense reserves are reasonable.

(3) Excess of Statutory Reserves Over Statement Reserves

Pursuant to California Insurance Code Section 11558, the outstanding loss and loss adjustment expense reserves for the most recent three years cannot be less than 65 percent of the workers compensation insurance premiums earned during each such year less the amount already paid for losses and expenses incidental thereto incurred during each such year. The Company's carried reserves for loss and loss adjustment expenses for each of the most recent three years were below the statutory minimum by $2,145,000 as of December 31, 2004. An examination adjustment was made to correct the deficiency.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Subsequent Events (Page 2): It is recommended that the Company take measures to strengthen its information systems controls.

Management and Control – Management Agreements (Page 4): It is recommended that the Company comply with California Insurance Code Section 1215.5(b)(4).

Previous Report of Examination

Accounts and Records (Page 9): It was recommended that the Company continue to test the disaster recovery plan and develop a written and tested business continuity plan. It was also recommended that the Company continue to monitor the implementation of the recommendations for the control weaknesses that were noted in the Company's claims information systems vendor's information systems environment. The control weaknesses in the information systems that were noted in the prior examination have not been fully addressed.

ACKNOWLEDGMENT

The cooperation and assistance rendered by the officers and employees of the Company during the examination is hereby acknowledged.

Respectfully submitted,

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Ber Vang, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California